

# Over-indebtedness Monitoring Paper Q3 2005

## Introduction

As part of the strategy outlined in 'Tackling Over-indebtedness: Action Plan 2004'<sup>1</sup>, the DTI is committed to monitoring levels of over-indebtedness in the UK. This paper aims to provide a high level balanced summary of the evidence on the level of over-indebtedness. Information is drawn primarily from publicly available sources, although where appropriate we also refer to specific research. This paper covers information on the situation up to September 2005. The paper will be updated quarterly to reflect the most recent information with the next paper covering Q4 2005 due to be published in March.

## Summary

Whilst the growth in consumer lending is lower than in 2004, there are some signs that a small but growing number of consumers are having problems repaying their borrowing. Mortgage arrears and mortgage possession orders continue to rise, albeit from low bases, and personal insolvencies across the UK continue their increasing trend. Despite this, few people on repayment plans are reporting difficulties with their repayments. Low interest rates and a healthy labour market continue to minimise the likelihood that those already borrowing will experience difficulty in the short term.

Bank write-offs continue to rise in Q3 2005, fuelled predominantly by consumer debt. However, the write-off rate on household lending is still low by historical standards. Of greater concern are the longer-term vulnerabilities such as the high debt-to-income ratio for the household sector.

## Notable changes since Q2 2005:

- Personal insolvencies in England and Wales grew by 11.6% on the previous quarter and 46.0% compared to the same period a year ago.
- Scottish sequestrations reached a series high of 1,461 in Q3 2005, an increase of 12% on the previous quarter.
- Average Q3 monthly repayments of consumers on repayment plans increased 11.9% on 2004 levels.

## This Report splits the evidence into three sections:

1. Macroeconomic Environment
2. Objective Measures of Over-indebtedness
3. Subjective Measures of Over-indebtedness

## Annex A: List of Data Sources

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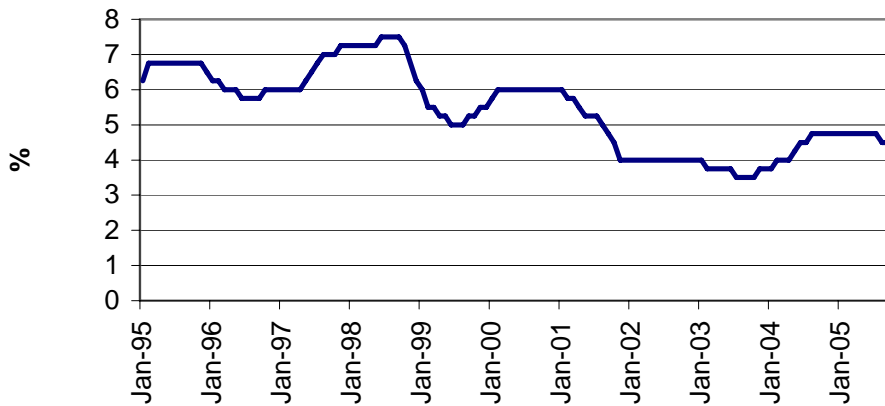
<sup>1</sup> Available at <http://www.dti.gov.uk/ccp/topics1/pdf1/overdebt0704.pdf>

# 1. Macroeconomic Environment

## 1.1 Interest Rates

During the Q3 2005 the Bank of England reduced the base rate by 0.25% to 4.5%. This is the first change to the base rate since August 2004. The cost of borrowing continues to stay relatively low by historic levels, however the continuing decline the growth rate of borrowing gives an indication that the rate increases throughout the first half of 2004 are beginning impact consumer behaviour.

**Figure 1: Base Rate<sup>2</sup>**

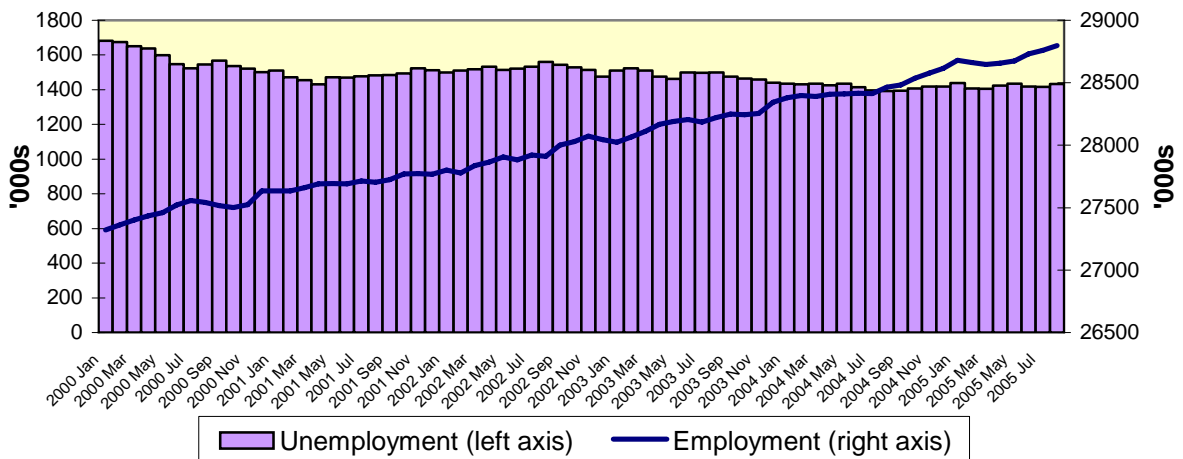


Source: Bank of England: Monetary & Financial Statistics Interactive Database

## 1.2 Labour Market

The risk to consumer over-indebtedness from forces in the labour market remains low. The UK labour market remains strong with a slight increase in the rate of employment growth over the last quarter. Measures of unemployment have remained relatively static over the last year and are at their lowest points for 20 years. Growth in employment has increased slightly in Q3 2005, the employment rate rising by 0.1% from July to August.

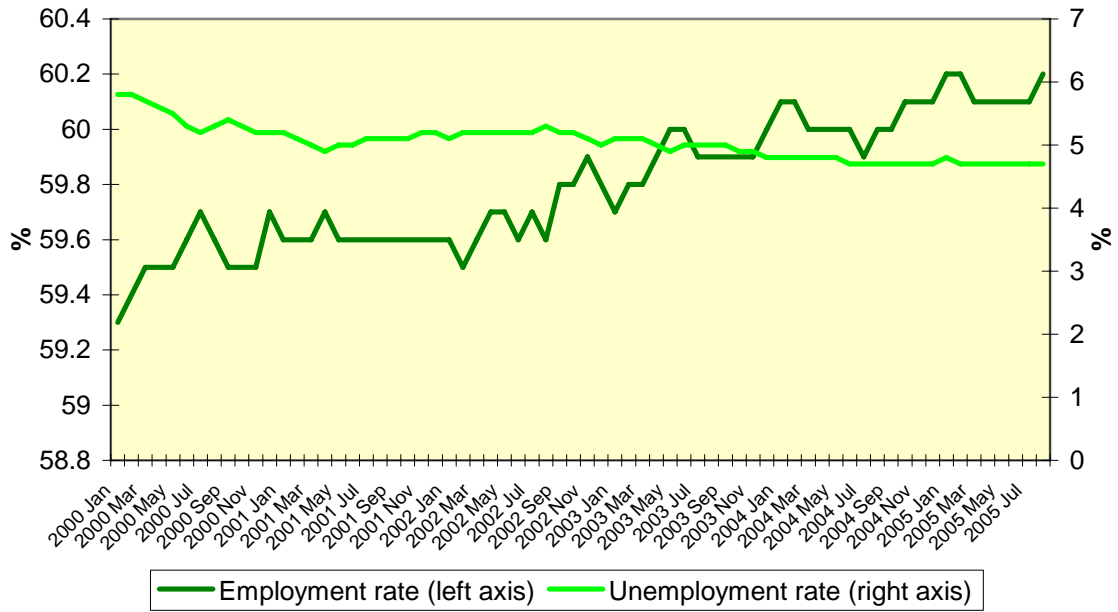
**Figure 2: Employment and Unemployment ('000s)**



Source: MGRZ and MGSC, ONS Labour Market trends

<sup>2</sup> IUMBEDR- End Month, Bank of England Repo Rate

**Figure 3: Employment and Unemployment Rates**

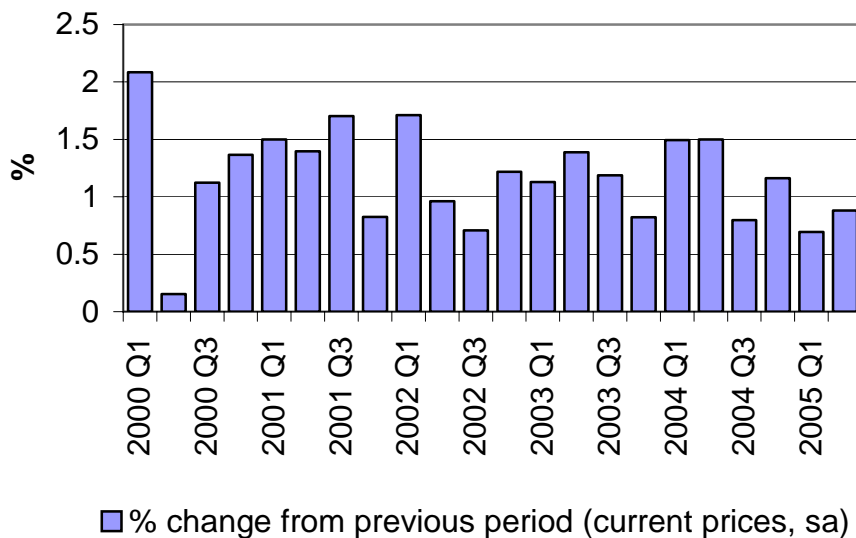


Source: MGSR and MGSX, ONS Labour Market trends

### 1.3 Consumer spending

Data on consumption growth for Q2 2005 shows a slight increase in the rate of growth to 0.9% from a four year low of 0.7% in Q1 2005. Growth in household consumer expenditure continues to be lower than average over the last five years, although Q2 growth indicates that the situation is improving. Data is not yet available for Q3 2005.

**Figure 4: Growth in Household Final Consumer Expenditure**



Source ONS: Consumer trends: Quarterly change in ABJQ

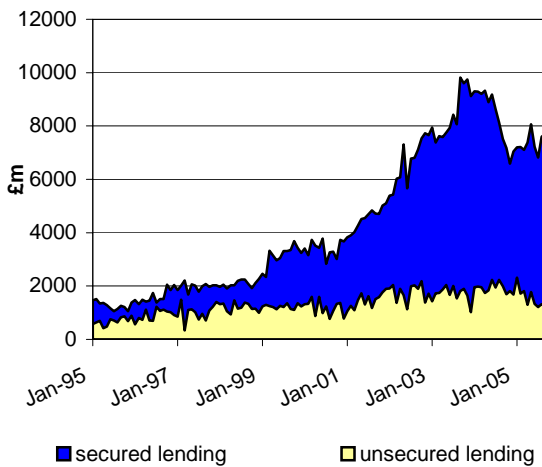
## 1.4 Consumer lending

Total lending to consumers continued to grow in Q3 2005 and the rate of growth has increased slightly on Q2 2005 levels.

Growth in the last quarter has been more pronounced in secured lending than in unsecured lending, where the growth rate has increased by 1.5% between August 2005 and September 2005. The increase in unsecured lending in September was 5.4% down on August and lower than the sixth month average.

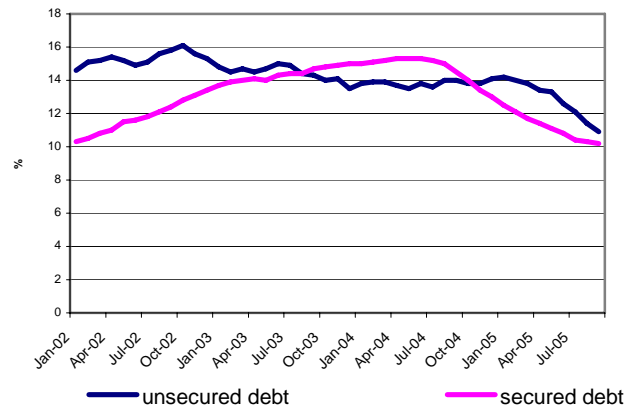
The rate of growth of total consumer lending has declined since Q3 2004 on all measures. Figures from the Bank of England show that the fall in growth over the last year has been more pronounced in secured lending than unsecured.

**Figure 5: Monthly changes to net lending £ millions**



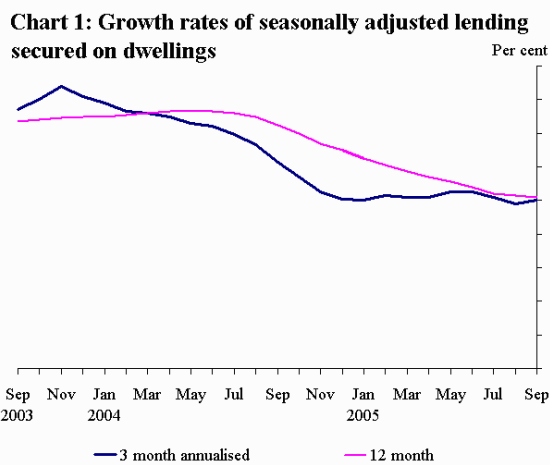
Source: Bank of England: LPMRLMH and LPMVTVJ

**Figure 6: 12 month growth rate of Net Lending**



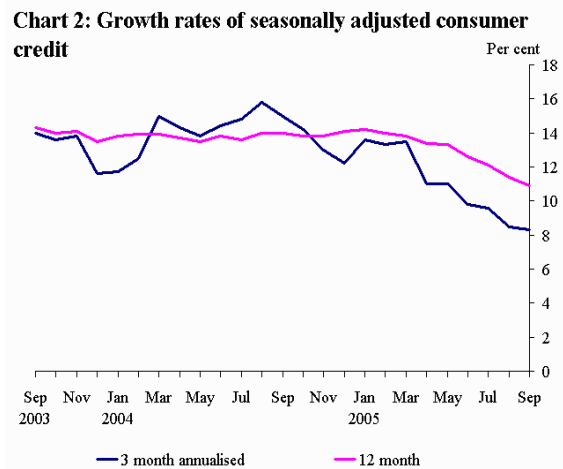
Source: Bank of England: LPMVTYO and LPMVTYI

**Figure 7: Growth in secured lending**



Source: Bank of England: Monetary & Financial Statistics Interactive Database

**Figure 8: Growth in unsecured lending**



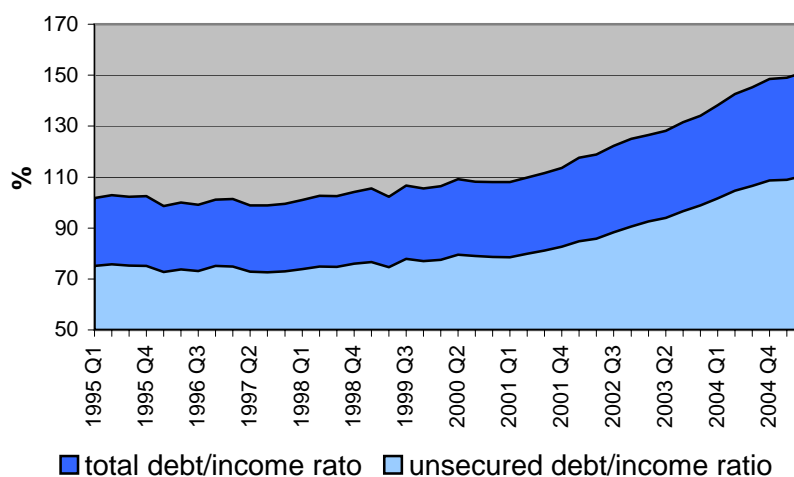
Source: Bank of England: Monetary & Financial Statistics Interactive Database

## 2. Objective measures of debt

### 2.1 Debt/Income Ratios

The growth rate of borrowing continued to outstrip that of earnings in Q2 2005, pushing up the total debt to income ratio to over 150% of annual income, a series high. The rate of growth in the last quarter is greater than that in Q1 2005 due to increases the rate of growth of secured borrowing. Data is currently unavailable for Q3 2005.

**Figure 9: Total Household Sector Debt / Income Ratios**



Source: ONS

### 2.2 Debt Write-offs

A number of large UK banks have recently declared an increase in their provisions for bad debt in 2005, whilst others have indicated actual rises in bad debt provisions. Barclays, for example, have recently indicated that bad debt provisions rose by 20% in the first half of the year to £706m<sup>3</sup>.

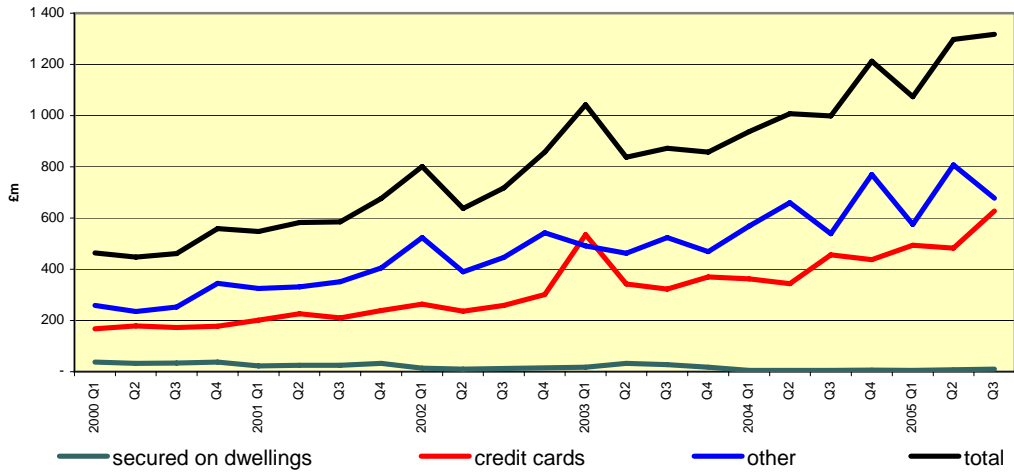
This correlates with figures for overall debt write offs for individuals, which show a gradual increase in write-offs over the past few years. Total write-offs to individuals in Q2 2005 increased by 28.7% year on year<sup>4</sup> (Q3 information is not yet available). Unsecured lending to UK households accounts for the largest domestic contribution to UK bank write-offs in recent years.

Such an increase could be expected as a result of the recent rise in personal insolvencies, but Figure 11 shows that growth in household write-offs has not quite matched that of personal insolvencies.

<sup>3</sup> Barclays interim financial report released 6 August 2005

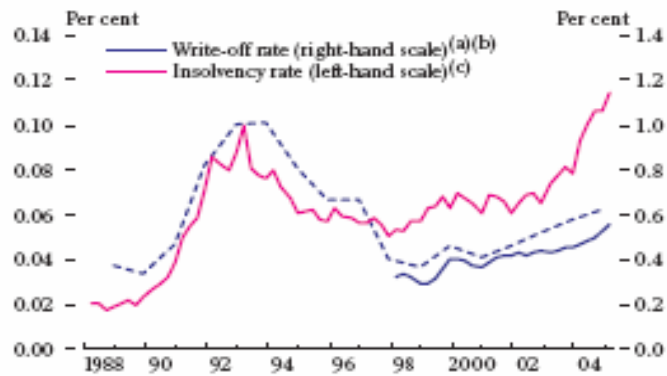
<sup>4</sup> The data series are variable because some lenders wait for their write-offs to consolidate before declaring them.

**Figure 10: Debt write-offs for individuals**



Source: Bank of England. Monetary & Financial Statistics August 2005, Table C2.1

**Figure 11: Household write-offs versus Insolvency rates**



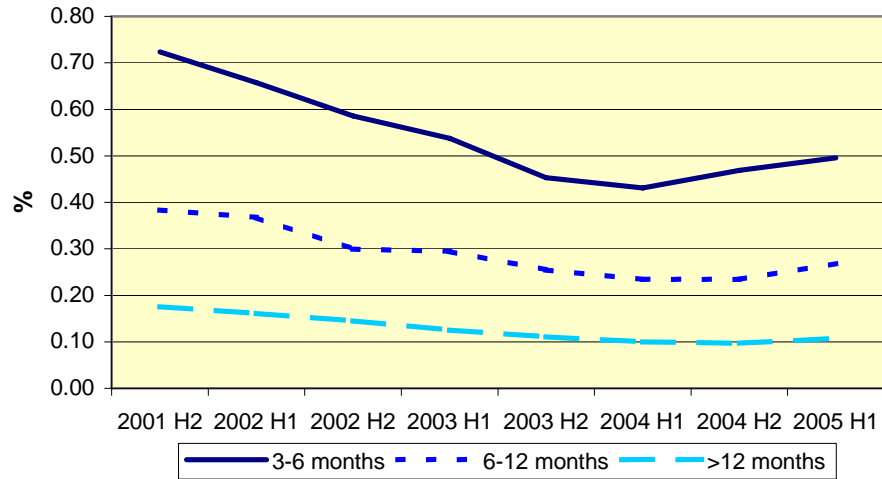
Sources: ONS, DTI and Bank of England.

- (a) Solid line shows annual write-off rate for UK-owned banks, dotted line the rate for all UK-resident banks (interpolated annual data).
- (b) Data are for individuals; unincorporated businesses excluded.
- (c) Data are for England and Wales, and are annualised.

## 2.3 Mortgage Arrears

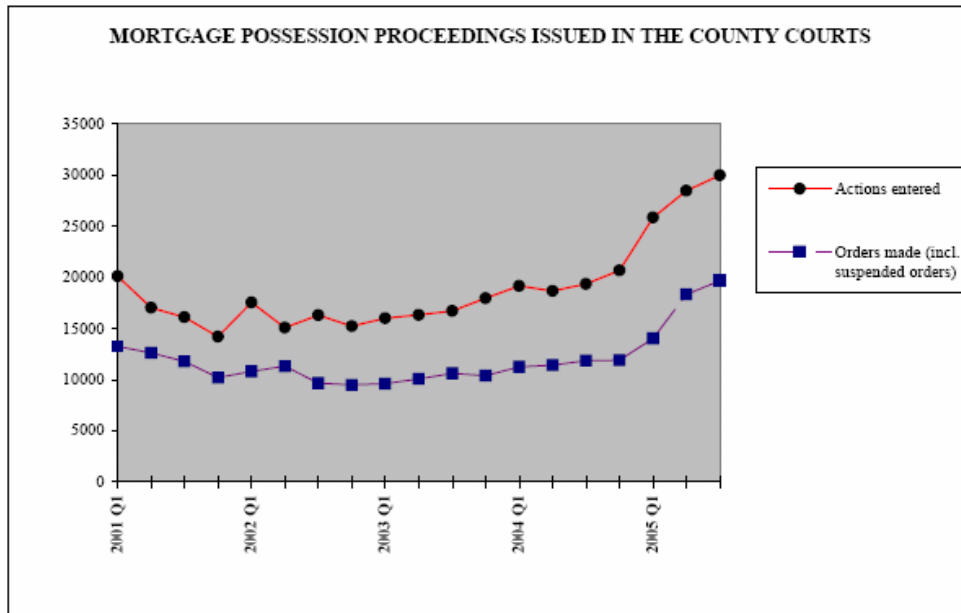
Mortgage arrears increased slightly over the first half of 2005, after increasing for the first time in 6 years in the second half of 2004. Mortgage possession actions continued to rise in Q3 2005, albeit at a slower rate, following sharp rises in Q1 and Q2. However, both series are still relatively low by historic standards.

**Figure 12: Mortgage arrears\***



\*Percentage of outstanding stock of mortgages.  
 Source: Council of Mortgage Lenders.

**Figure 13: Mortgage possession orders**



Source: Department of Constitutional affairs

## 2.4 Those over-indebted accessing professional services as a result of over-indebtedness

### 2.4.2 Personal insolvency

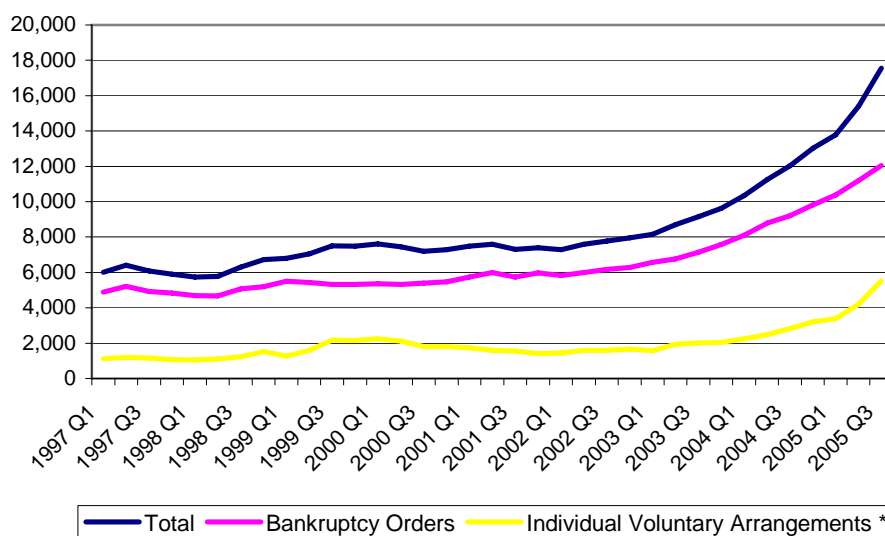
A number of statutory instruments are available to individuals facing serious financial difficulty, which include;

- Bankruptcy/Sequestration (Scotland)
- Individual Voluntary Arrangements (IVA's)
- Fast Track Individual Voluntary Arrangements
- County Court Administration Orders

There were 17,562 bankruptcies and IVA's in England and Wales in the Q3 2005 on a seasonally adjusted basis. This was an increase of 11.6% on the previous quarter and an increase of 46.0% on the same period a year ago.

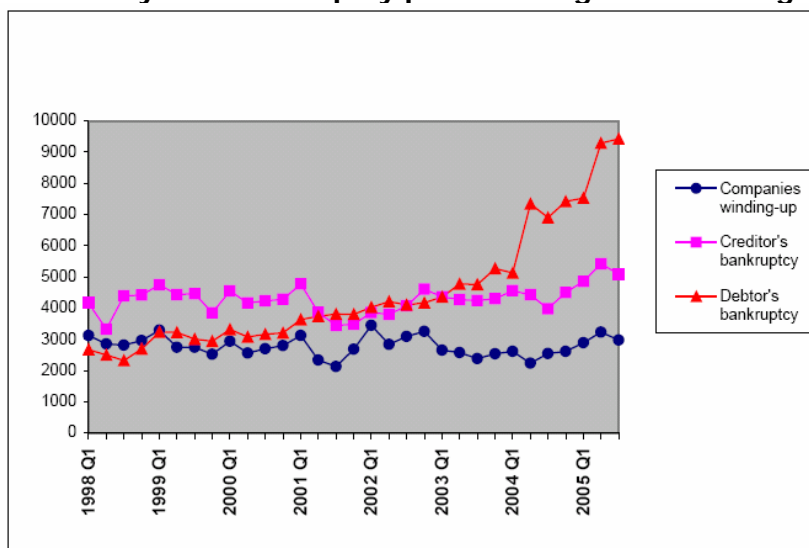
This was made up of 12,043 bankruptcies, an increase of 6.0% on the previous quarter and 30.9% on the corresponding quarter of last year, and 5,519 IVA's, an increase of 26.1% on the previous quarter and an increase of 95.0% on the corresponding quarter of the previous year. The take up of Fast Track voluntary arrangements has been extremely low and are included in the figures for IVA's.

**Figure 14: Individual Bankruptcies and IVA's in England & Wales ('000s)**



Source: Insolvency service, DTI  
\*Includes deeds of arrangement

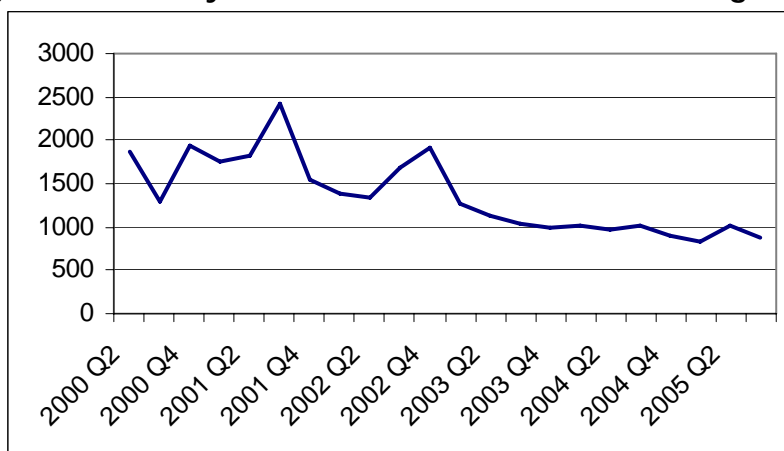
**Figure 15: Insolvency and Bankruptcy petitions registered in England & Wales**



Source: Department for Constitutional Affairs.

Information on the number of County Court Administration Orders (AO's) indicates that their numbers are low and continuing to decrease. This is due entirely to the current debt limit (£5k), which is set in statute, and means AO's are not relevant for most consumers entering insolvency proceedings.

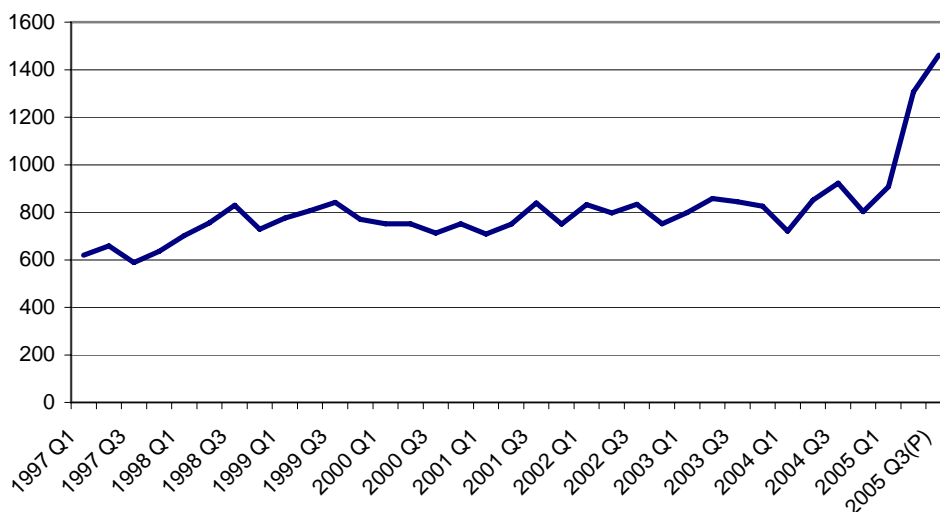
**Figure 16: County Court Administration Orders in England & Wales**



Source: Department for Constitutional Affairs.

Sequestrations in Scotland increased markedly in Q2 2005, and to a lesser extent in Q3, according to provisional results. Figures released in November cite a rise from 923 to 1,461 in Q3 2004, an increase of 58% year on year. This is explained by a rapid rise in creditor petitions since April following a crack down by Scottish councils on individuals with persistent council tax arrears beginning in Q2.

**Figure 17: Sequestrations in Scotland**



Source: DTI Statistics

In addition to these statutory instruments a number of non-statutory options exist for individuals in financial difficulty such as debt renegotiation, re-mortgaging and Debt Management Plans (DMPs). Due to the fact that they are non-statutory and not provided by a single source it is difficult to assess the number of individuals taking such action. DTI is working in collaboration with other partners to try to identify the number of DMP's currently provided to over-indebted consumers.

## 2.4.2 key drivers

Personal insolvency levels can and do fluctuate. There is no conclusive evidence of a single driver that might be contributing to the overall increase in personal insolvencies, although research generally attributes changes in bankruptcy numbers to economic factors, in particular availability and levels of credit, although asset/debt ratios, interest rates and employment levels all play a part.

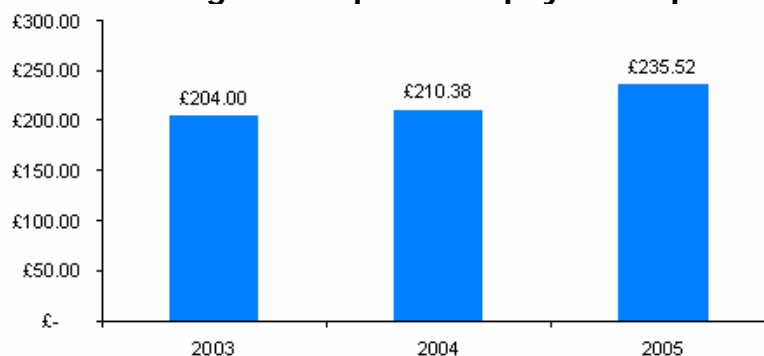
As previously reported, the Insolvency Service is continuing to evaluate the effect of the changes to the personal insolvency regime brought about by the Enterprise Act 2002, but it appears that the changes in legislation have had little if any effect on the number of people becoming bankrupt. The continued rise in the number of individual voluntary arrangements, where there has been no legislative change, and which is in percentage terms is greater than the increase in bankruptcy numbers, suggests that the increases in personal insolvency levels are being influenced by factors other than changes in the law.

The Insolvency Service will shortly publish a report on basic bankruptcy profiling for the years 2001/2 to 2004/5 covering gender, age, number of creditors and debt levels, based on population counts, with a more detailed report on bankruptcy characteristics for 2002/3 to 2004/5 to be published during the summer of 2006.

## 2.5 Debt repayment

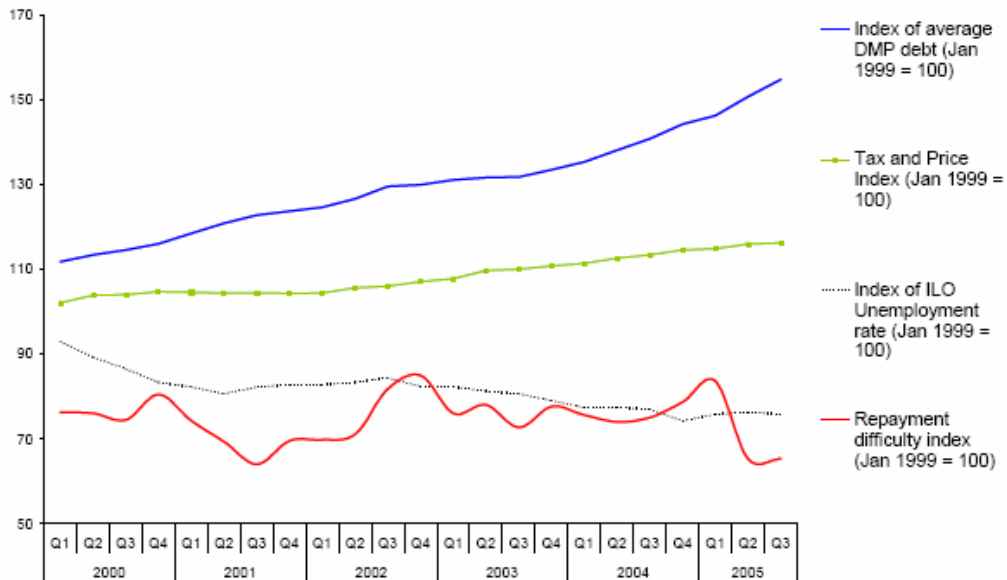
Data released by the Consumer Credit Counselling Service in September 2005 indicates that average Q3 monthly client repayments reached £235 in 2005, an increase of 11.9% on 2004 levels.

**Figure 18: Average third quarter repayments per month**



In terms of the difficulty of repayment, the CCCS index remained constant at Q2 levels and at a historically low level in Q3. The index fell 12% year on year from quarter two of 2004 (65.3). It has now reached the second lowest quarterly figure since the index began.

**Figure 19: CCCS repayment difficulty index**



**Notes**

1) Tax and Price Index measures how much the average person's gross income needs to change to purchase the RPI basket after allowing for the average amount of income tax and national insurance paid on earnings.

### 3. Subjective measures of debt

Survey results on consumers' from the DTI commissioned MORI Financial Services survey (2004) show only a small proportion (5%) of debtors consider their debt repayments a heavy burden. This survey is next due to be undertaken in 2006 and published in early 2007.

The results broadly consistent with similar research from the Bank of England, which shows that the number of borrowers who declared their unsecured debt repayments a 'heavy burden' has remained relatively constant over the past decade, where the most recent survey information was published in September 2004.

## Annex A: List of Data Sources relevant to Consumer Over-Indebtedness

The release date of each data series varies according to publication, to find out the release date of a specific series it is best to check the relevant link. In general, monthly data are available at the end of the following month and quarterly data as follows; Q1= Early April, Q2= Early July, Q3= Early October, Q4= Early Jan.

Frequency key: D= Daily, M= Monthly, Q= Quarterly, A= Annual.

Measure	Source	Frequency	When available	Weblink
<b>Base Rate</b> (Underlying Interest Rate)	Bank of England: Monetary & Financial Statistics Interactive Database	D, M, Q, A	1 <sup>st</sup> week of every month.	<a href="http://213.225.136.206/mfsd/iadb/Index.asp?first=yess&amp;SectionRequired=I&amp;HideNums=-1&amp;ExtraInfo=true&amp;Travel=Nlx">http://213.225.136.206/mfsd/iadb/Index.asp?first=yess&amp;SectionRequired=I&amp;HideNums=-1&amp;ExtraInfo=true&amp;Travel=Nlx</a>  Click 'Wholesale Interest and Discount Rates' then 'Bank of England repo rate (base rate)'
<b>Employment (MGRZ) and Unemployment (MGSC) Employment rate (MGSR) and Unemployment Rate (MG SX)</b>	Office for National Statistics: Labour Market trends Seasonally Adjusted figures	M, Q, A	Check:  <a href="http://www.statistics.gov.uk/statbase/tsdreleasedates.asp">http://www.statistics.gov.uk/statbase/tsdreleasedates.asp</a>	<a href="http://www.statistics.gov.uk/statbase/tsdtimezone.asp">http://www.statistics.gov.uk/statbase/tsdtimezone.asp</a>  Select 'Labour Market stats' then 'Unemployment by age and duration' and 'Employment by age'
<b>Growth in Household Final Consumer Expenditure</b>	Office for National Statistics: Consumer trends: Quarterly change in ABJO	Q	Check:  <a href="http://www.statistics.gov.uk/statbase/tsdreleasedates.asp">http://www.statistics.gov.uk/statbase/tsdreleasedates.asp</a>	<a href="http://www.statistics.gov.uk/statbase/tsdtimezone.asp">http://www.statistics.gov.uk/statbase/tsdtimezone.asp</a>  Select 'Consumer Trends then 'O.CS: Household Final Consumer Expenditure'
<b>Monthly changes to net lending £ millions</b>	Bank of England: LPMRLMH and LPMVTVJ	M	End of following month	<a href="http://213.225.136.206/mfsd/iadb/NewIntermed.asp">http://213.225.136.206/mfsd/iadb/NewIntermed.asp</a>  Search for 'LPMRLMH' and 'LPMVTVJ'
<b>Growth in unsecured lending</b>	Bank of England: Monetary & Financial Statistics Interactive	M	End of following month	<a href="http://213.225.136.206/statistics/li/current/index.htm">http://213.225.136.206/statistics/li/current/index.htm</a>

	Database			
<b>12 month growth rate of Net Lending</b>	Bank of England: LPMVTYO and LPMVTYI	M	End of following month	<a href="http://213.225.136.206/mfsd/iadb/NewIntermed.asp">http://213.225.136.206/mfsd/iadb/NewIntermed.asp</a>  Search for 'LPMVTYO' and 'LPMVTYI'
<b>Growth in lending secured on dwellings</b>	Bank of England: Monetary & Financial Statistics Interactive Database	M	End of following month	<a href="http://213.225.136.206/statistics/li/current/index.htm">http://213.225.136.206/statistics/li/current/index.htm</a>
<b>Total Household Sector Debt / Income Ratios</b>	Office for National Statistics: Total Debt / Income Ratio (NNPP/4*RPOK) Secured Debt / Income Ratio (NNRP/4*RPOK)	Q	Check:  <a href="http://www.statistics.gov.uk/statbase/tsdreleasedates.asp">http://www.statistics.gov.uk/statbase/tsdreleasedates.asp</a>	<a href="http://www.statistics.gov.uk/statbase/tsdtimezone.asp">http://www.statistics.gov.uk/statbase/tsdtimezone.asp</a>  Select 'Financial Consistent' and go to table 12.1N for NNPP, table 9.1M for NNRP and table 14.8D for RPOK
<b><i>UK Bank Write-offs</i></b>	Bank of England. Monetary & Financial Statistics August 2005, Table C2.1 (TFHD, TFHE, TFHF, TFHG)	A		<a href="http://www.bankofengland.co.uk/statistics/ms/current/index.htm - c">http://www.bankofengland.co.uk/statistics/ms/current/index.htm - c</a>
<b><i>Mortgage arrears</i></b>	Council of Mortgage Lenders.	A, Half- Yearly		<a href="http://www.cml.org.uk/servlet/dycon/zt-cml/cml/live/en/cml/stats_free">http://www.cml.org.uk/servlet/dycon/zt-cml/cml/live/en/cml/stats_free</a>  <a href="#">Mortgage arrears, by number of months in arrears</a> <a href="#">Mortgage arrears, by percentage of total balance in arrears</a>
<b>Mortgage possession orders</b>	Department for Constitutional Affairs.	Q		<a href="http://www.dca.gov.uk/statistics/cjust.htm">http://www.dca.gov.uk/statistics/cjust.htm</a>
<b>Individual Insolvencies in England &amp; Wales ('000s)</b>	Insolvency service, DTI	Q		<a href="http://www.dti.gov.uk/statistics/index.htm">http://www.dti.gov.uk/statistics/index.htm</a>  Scroll down to Insolvency statistics
<b>Sequestrations in Scotland</b>	Insolvency service, DTI	Q		<a href="http://www.dti.gov.uk/statistics/index.htm">http://www.dti.gov.uk/statistics/index.htm</a>

				Scroll down to Insolvency statistics
<b>Bankruptcy petitions registered in England &amp; Wales</b>	Department for Constitutional Affairs.	Q		<a href="http://www.dca.gov.uk/statistics/cjust.htm">http://www.dca.gov.uk/statistics/cjust.htm</a>
<b>County Court Actions</b>	Department for Constitutional Affairs.	Q	End of following month	Not publicly available.
<b>CCCS debt repayment/repayment difficulty index</b>	CCCS	Q		<a href="http://www.cccs.co.uk/media/media.aspx">http://www.cccs.co.uk/media/media.aspx</a> Link usually embedded in press releases. Look for <a href="#">Debt Dashboard Q4 2004 (PDF)</a>
<b>Burden of Debt</b>	MFS survey, Bank of England	Varies.	Bank of England Autumn 2005 DTI Survey Autumn 2006	MFS Study available: <a href="http://www.dti.gov.uk/ccp/topics1/overindebtedness.htm">http://www.dti.gov.uk/ccp/topics1/overindebtedness.htm</a> Check publications for 2005 update. <a href="http://213.225.136.206/publications/index.htm">http://213.225.136.206/publications/index.htm</a>

Department of Trade and Industry  
Consumer and Competition Policy Directorate

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